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C O N F I D E N T I A L SECTION 01 OF 02 BAGHDAD 002820

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SUBJECT: GOI AUCTIONS TELECOMS LICENSES FOR USD 3.75 BILLION AMID CRIES OF FOUL AND CHALLENGES TO THE DEAL'S FINALIZATION

REF: A. A. BAGHDAD 02524

1B. B. BAGHDAD 2402

Classified by Economic Minister Charles P. Ries for reasons 1.4(b) and (d).

11. (C) SUMMARY: The GOI auctioned three 15-year mobile telecommunications licenses, each one fetching USD 1.25 billion up front, plus 18.5 percent of monthly gross revenues and 15 percent of net profits. Two of three incumbents--Asiacell and MTC Atheer--won new licenses, and Korek Telecom won the third, potentially enabling it to expand its heretofore Kurdish regional operations. The third incumbent, Orascom Telecom, owner of central Iraq's Iraqna network, withdrew as the bidding climbed; Orascom is out, but the future of its Iraqna assets remains unclear. The auction's results were mixed: the licenses garnered five times the price the GOI had negotiated with the operators in March 2007, but the process elicited cries of foul from observers. A member of Iraq's Council of Representatives (CoR) claimed the auction was unconstitutional, alleged irregularities, and vowed to undo the deal legislatively when the CoR returns from recess in September. The price the licenses commanded evidenced some investors' willingness to make substantial, long-term commitments in currently profitable sectors of the Iraqi economy, but the high prices paid will be difficult to amortize over the medium term. Moreover, despite the involvement of Pricewaterhouse Coopers (PwC), there are real questions about the transparency of the process and uncertainties about whether the licenses will be finalized as negotiated. These questions may mean the auction's results do little to make Iraq more attractive to outside investors. END SUMMARY.

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LICENSES FETCH MORE THAN EXPECTED  
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12. (C) Originally scheduled for September 2006, Finance Minister Jabr chaired the auction, which took place in Amman, Jordan, August 19-20, overseen by PwC. Representatives of Iraq's Ministries of Finance, Planning, Communication, and Science & Technology, as well as the Communications and Media Commission (CMC), the Board of Supreme Audit, the Commission on Public Integrity, and the CoR attended. The GOI had hoped a dozen firms would participate, but only five did: Sulimaniya-based Asiacell; Baghdad-based MTC Atheer, owned by MTC of Kuwait; Cairo-based Orascom Telecom; Irbil-based Korek; and, Istanbul-based Turkcell. Bidding began at USD 325 million per license, and Jabr held eighteen additional rounds at USD 50 million increments. Turkcell withdrew at USD 950 million, and Orascom at USD 1.15 billion.

13. (C) In the end Asiacell, MTC Atheer, and Korek took the following terms: a lump sum USD 1.25 billion to be paid within one month of the auction; 18.5 percent of monthly gross revenues; and a 15 percent tax on corporate net

profits. Subscribers will also pay a .25 percent tax for universal service and .25 percent for number portability. Jabr publicly estimated that the licenses would bring the GOI roughly USD 8 billion over fifteen years. The final license price was five times that negotiated between the GOI and the incumbent operators in March 2007. Several auction attendees claimed that Jabr stated the evening beforehand he intended to return to Baghdad with USD 3 billion (NOTE: Saudi Arabia recently sold a license for USD 6.1 billion, and Egypt one for USD 2.9 billion. END NOTE)

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CONCERNS FOR LACK OF TRANSPARENCY PROVE JUSTIFIED  
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¶4. (C) CoR members objected when the GOI announced plans to hold the auction in Amman, expressing concerns over a lack of transparency and potential corruption (reftel A). Evidence suggests their concerns were justified. A CoR member attending the auction claimed the auction was unconstitutional, arguing that the CoR removed executive power from the CMC, which had contracted PwC to manage the event, in September 2006. The member stated that undoing the auction through legislation would be a top priority for the CoR when it resumes session in September. In a separate meeting with EconOffs, CoR Member Yonadam Kanna--Chairman of the CoR's Economy, Investment & Reconstruction Committee--stated that because Korek was owned by the powerful Barzani family the firm received undue favorable consideration. (NOTE: Kanna otherwise described the auction as a success. END NOTE) Asiacell, for its part, sent a letter to Prime Minister Nuri al Maliki arguing that Korek's participation in the auction was improper because it did not meet the requisite financial criteria by the date set forth

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in the bidding documents. Asiacell stated it may challenge Korek's participation in Iraq's courts.

¶5. (C) Others complained about Jabr's chairing of the process itself. The CMC had worked with PwC on safeguards to ensure an orderly affair, but Jabr overrode several of them in the event. Under the rules, once the license fee reached USD 500 million bidding was to have switched to the regulatory fee, starting at 18.5 percent, but Jabr forged ahead to the ultimately agreed USD 1.25 billion. In addition, a break was scheduled for 20:00 on August 19, to give the participants an opportunity to rest and review the terms, but Jabr pushed through to 04:00 the morning of August 20. Jabr also added the 15 percent net profits tax to the terms on the day of the auction. Winning bidders have stated that they will raise consumer prices by as much as 60 percent to compensate for the additional charges.

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THE FATE OF ORASCOM'S IRAQNA ASSETS REMAINS UNCLEAR  
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¶6. (C) Jabr stated that he was surprised when Orascom withdrew. Telecoms analysts estimate the firm had invested USD 300 million in its Baghdad-centered Iraqna network, and Orascom itself claimed to have approximately 3 million subscribers. On August 19, Orascom representatives stated that the firm was "evaluating alternatives" with respect to its Iraqna assets. A high-level GOI official said, however, that within hours of the auction's conclusion, MTC Atheer agreed to buy the Iraqna equipment and customer accounts for USD 1.25 billion. The GOI official further stated that no announcement would be made until the two firms finished a due diligence review of the deal. Media sources report that both MTC Atheer and Korek are in talks with Orascom to buy Iraqna assets.

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COMMENT  
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¶7. (C) In addition to CoR members' threats to undo the deal legislatively, business concerns also threaten its finalization. Korek based its strategy for expanding beyond Iraqi Kurdistan on acquiring Iraqna's network and customer base. If MTC Atheer concludes its reported purchase of Iraqna's assets, Korek might renege and simply remain in its established Kurdish regional market. Korek's withdrawal would leave only Asiacell and MTC Atheer in Iraq's mobile telecoms market. Industry sources in Dubai and Zurich also report that MTC Atheer's parent company, MTC Kuwait, is discussing selling itself to Saudi Telecom, and Iraq presently has no telecommunications or competition law to prevent either MTC Atheer or Saudi Telecom from purchasing Asiacell and monopolizing the Iraqi mobile telecommunications market. Such concerns could further encourage CoR intervention.

¶8. (C) The good news from the auction is that it evidenced some investors' willingness to commit billions of dollars to long-term plans in sectors of the Iraqi economy believed profitable, despite the ongoing security challenges. (NOTE: Iraq has an estimated 8-10 million mobile telephone subscribers out of an estimated population of 27.5 million, up from a pre-war level of near zero, and analysts project demand to grow. END NOTE) But the story is not all roses: the funds derived from the auction will go directly to Ministry of Finance coffers, and it is unclear how much of the auction's proceeds will be available to be invested in the telecommunications sector that generated them. More important, the auction process--tainted by irregularities, eleventh-hour changes to terms, and allegations of political interference--did nothing to make Iraq more attractive to outside investors.

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